

Chapter 4

Guidance on regulated activities connected with mortgages

4.4 What is a regulated mortgage contract?

The definition of "regulated mortgage contract".....

4.4.1

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Article 61(3)(a) of the *Regulated Activities Order* defines a *regulated mortgage contract* as a contract which, at the time it is entered into, satisfies the following conditions:

- (1) the contract is one where a lender provides credit to an individual or trustees (the 'borrower');
- (2) the contract provides for the obligation of the borrower to repay to be secured by a mortgage on land in the *EEA*; and
- (3) at least 40% of that land is used, or is intended to be used, as or in connection with a dwelling.

This section sets out the *FCA's* understanding of some key concepts contained in article 61(3)(a). It should be noted that, where a contract meets the necessary requirements for both a *regulated mortgage contract* and a *home purchase plan*, it will be treated as a *home purchase plan* only and will not be a *regulated mortgage contract*. Guidance on the meaning of a *home purchase plan* is in ■ PERG 14.4 (Guidance on home reversion and home purchase activities).

4.4.1-A

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A contract is not a *regulated mortgage contract* if it is:

- (1) a loan to a commercial borrower excluded under ■ PERG 4.4.17 G or ■ PERG 4.4.21 G; or
- (2) a second charge loan by a credit union excluded under ■ PERG 4.4.24 G; or
- (3) a second charge bridging loan excluded under ■ PERG 4.4.27 G;
- (4) a *CBTL credit agreement* excluded as described in ■ PERG 4.4.31G.

Provision of credit.....

4.4.1A

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- (1) Article 61(3)(c) of the *Regulated Activities Order* states that credit includes a cash loan and any other form of financial accommodation. Although 'financial accommodation' has a potentially wide meaning, its scope is limited by the terms used in the definition of a *regulated mortgage contract* set out in ■ PERG 4.4.1 G. Whatever form the financial accommodation may take, article 61(3)(a) envisages that it

must include an obligation to repay on the part of the individual who receives it.

- (2) In the *FCA's* view, an obligation to repay implies the existence, or the potential for the existence, of a debt owed by the individual to whom the financial accommodation is provided (the 'borrower') to the *person* who provides it (the 'lender').
- (3) For example, a bank would be providing 'credit' which, subject to the other requirements being met, could amount to a *regulated mortgage contract* if it gives a guarantee that:
 - (a) creates a debt or a potential debt; and
 - (a) allows for deferred payment.

Which borrowers?

4.4.2

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The condition set out in ■ PERG 4.4.1G (1) limits the range of borrowers to whom the protections of the mortgage regulation regime apply to individuals and trustees. If a *company* (which is not acting as a trustee) borrows money for the purpose of funding the *company's* business, and the loan is secured by a mortgage over the *company's* property, the mortgage contract is not a *regulated mortgage contract*. So a lender will not carry on a *regulated activity* by entering into that contract, nor will the lender carry on a *regulated activity* if it advises on, arranges or administers that contract. However, if the lender makes a loan for business purposes to an individual sole trader, or (in England and Wales) a partnership, and the loan is secured on the borrower's house or houses, the contract will be a *regulated mortgage contract*.

4.4.2A

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- (1) A loan to a trustee is caught, even if the trustee or the beneficiary is not an individual.
- (2) Therefore, it is possible that a loan to a trustee acting for a large commercial *company* is a *regulated mortgage contract*.
- (3) In practice, the exclusions for loans to commercial borrowers (in particular, see ■ PERG 4.4.17 G and ■ PERG 4.4.21 G) are likely to prevent such loans from being *regulated mortgage contracts*.
- (4) If:
 - (a) the loan is made to a trustee;
 - (b) the trustee is a bare trustee or nominee; and
 - (c) the beneficiary of the trust is acting for commercial purposes;
 it is likely that the trustee will also be acting for commercial purposes.

4.4.2B

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A loan to a partnership may be a loan to an individual if the partnership is made up of real people (that is natural, as opposed to legal, *persons*).

Date the contract is entered into

4.4.3 **G** In order to meet the definition of a *regulated mortgage contract*, a mortgage contract must meet the conditions set out in ■ PERG 4.4.1G (1) to ■ PERG 4.4.1G (3) at the time it was entered into. The effect is that contracts which meet those conditions at that time remain *regulated mortgage contracts* throughout their remaining term, even if there are periods of time when some or all of the conditions are not satisfied. Conversely, contracts that do not start out as *regulated mortgage contracts* cannot subsequently become so, even if they meet all the conditions set out in ■ PERG 4.4.1G (1) to ■ PERG 4.4.1G (3). A *person* that only administers mortgage contracts which did not meet those conditions at the time they were entered into will not, therefore, need *permission* to administer *regulated mortgage contracts*.

4.4.4 **G** There may, however, be instances where an existing contract, which was not a *regulated mortgage contract* at the time it was entered into, is replaced as a result of a variation (whether the variation is initiated by the customer or by the lender), and the new contract qualifies as a *regulated mortgage contract*. A *person* may therefore need to consider this possibility (which could affect contracts initially entered into before 31 October 2004 as well as subsequent loans) when deciding whether he needs *permission* to carry on any of the *regulated mortgage activities*.

Land in the EEA

4.4.5 **G** The condition set out in ■ PERG 4.4.1G (2) means that a *regulated mortgage contract* must be secured on land in the *EEA*. Contracts which involve taking security over moveable property therefore cannot be *regulated mortgage contracts*. So a contract secured on a caravan will not be a *regulated mortgage contract*, unless the contract also involves a mortgage over the land on which the caravan stands.

Occupancy requirement

4.4.6 **G** The condition set out in ■ PERG 4.4.1G (3) means that loans secured on property which is entirely used for business purposes (such as an office block) cannot fall within the definition. However, loans secured on 'mixed use' property could be covered, provided that the occupier uses at least 40% of the total of the land as or in connection with a dwelling. Loans secured on a six-floor property, half of which was occupied by a family as their home and half let out for business purposes would therefore satisfy the definition. (Article 61(4)(b) makes it clear that 'land', in the context of a multi-storey building, means the aggregate of the floor area of each of the storeys.)

4.4.6A **G** The most obvious example of a *regulated mortgage contract* is a loan made to an individual to enable the individual to buy a home for themselves where the loan is secured on that home. However, there is no requirement that the borrower should occupy the property. There is a requirement that at least 40% of the land should be used as a house, but no requirement that it is the borrower who uses it as a house. So, for example:

- (1) a loan may be a *regulated mortgage contract* if the property on which it is secured is to be occupied by the borrower's relatives as their home; or

- (2) a loan may be a *regulated mortgage contract* if the borrower does not occupy the property on which the loan is secured and instead intends to sell the property to a third party, with the mortgage remaining on the house until then.
- (3) However, if the borrower is acting on a commercial basis, the loan in (2) may be excluded as a loan to a commercial borrower under the exclusions in ■ PERG 4.4.17 G or ■ PERG 4.4.21 G.
- (4) A buy-to-let loan secured on the property to be let is potentially a *regulated mortgage contract*. However, such a loan may be excluded as a loan to a commercial borrower under the exclusions referred to in (3) or under the buy-to-let exclusions described in ■ PERG 4.4.31G and ■ PERG 4.10B which refer to consumer borrowers.

4.4.7 **G** The expression 'as or in connection with a dwelling' set out in ■ PERG 4.4.1G (3) means that loans to buy a small house with a large garden would in general be covered. However, if at the time of entering into the contract the intention was for the garden to be used for some other purpose – for example, if it was intended that a third party were to have use of the garden – the contract would not constitute a *regulated mortgage contract*. Furthermore, the FCA would not regard a loan to purchase farmland and a farmhouse as constituting a *regulated mortgage contract* (where the farmhouse and garden amount to less than 40% of the land area), since it does not appear that the land could properly be said to be used 'in connection with' the farmhouse. The presence of the farmhouse is unconnected with the use to which the farmland is put (in contrast to a residential property's garden, which would have no existence independent of the property).

4.4.8 **G** [deleted]

4.4.9 **G** [deleted]

Purpose of the loan is irrelevant

4.4.10 **G** The definition of *regulated mortgage contract* contains no reference to the purpose for which the loan is being made. So, in addition to loans made to individuals to purchase residential property, the definition is wide enough to cover other loans secured on land, such as loans to consolidate debts, or to enable the borrower to purchase other goods and services.

Type of lending

4.4.11 **G** The definition of *regulated mortgage contract* also covers a variety of types of product. Apart from the normal mortgage loan for the purchase of property, the definition also includes other types of secured loan, such as secured overdraft facility, a *bridging loan* (although bridging loans described in ■ PERG 4.4.27 G are not *regulated mortgage contracts*), a secured credit card facility and *regulated lifetime mortgage contracts* under which the borrower (usually an older person) takes out a loan where repayment of the capital (and in some cases the interest) is not required until the property is sold, usually on the death of the borrower.

4.4.12 **G** Loans secured on commercial premises are not *regulated mortgage contracts* as the property will not be used as or in connection with a dwelling.

4.4.13 **G** [deleted]

4.4.14 **G** [deleted]

Type of security

4.4.15 **G** A loan may be a *regulated mortgage contract* whether it is secured by a first, second or subsequent mortgage.

4.4.16 **G** A mortgage has a wide meaning for the purpose of the definition of a *regulated mortgage contract*. It includes:

- (1) a legal mortgage;
- (2) equitable security;
- (3) (in Scotland) a heritable security; and
- (4) security commonly used in another *EEA State* for loans secured on residential property.

4.4.16A **G** It is possible for more than one mortgage contract to be secured by the same charge.

Exclusions for lending to commercial borrowers

4.4.17 **G** A contract is excluded from the definition of *regulated mortgage contract* if, at the time it is entered into, it meets the following conditions:

- (1) it meets the conditions in ■ PERG 4.4.1G (1) to ■ (3); and
- (2) less than 40% of the land secured by the mortgage is used, or intended to be used, as or in connection with a dwelling by the borrower or (for credit provided to trustees) by an individual who is a beneficiary of the trust, or by a *related person*; and
- (3) the agreement is entered into by the borrower wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by the borrower.

4.4.18 **G** The *Regulated Activities Order* refers to this as an "investment property loan".

4.4.19 **G** Under the *Regulated Activities Order* '*related person*' means, in relation to the borrower or (for credit provided to trustees) a beneficiary of the trust:

- (1) that *person's* spouse or civil partner;

- (2) a *person* (whether or not of the opposite sex) whose relationship with that *person* has the characteristics of the relationship between husband and wife; or

(3) that *person's* parent, brother, sister, child, grandparent or grandchild.
- 4.4.20** **G** (1) If less than 40% of the land secured by the mortgage is used, or intended to be used, as or in connection with a dwelling then the exclusion for loans to commercial borrowers described in **■ PERG 4.4.17 G** is irrelevant, as the loan falls outside **■ PERG 4.4.1 G** and so cannot be a *regulated mortgage contract*.

(2) The exclusion becomes relevant (if all the conditions in **■ PERG 4.4.17 G** are met) if at least 40% of the land secured by the mortgage is used, or intended to be used, as or in connection with a dwelling by:

 - (a) someone other than the borrower; or
 - (b) the borrower and someone else, if the percentage used by the borrower as residential property is less than 40%.

(3) Therefore, the exclusion would, for example, cover a loan secured on residential property where a commercial borrower is not going to occupy any of the property but is going to sell it to a third party.
- 4.4.21** **G** There is also an exclusion for loans to commercial borrowers secured by a second or subsequent security. A contract is excluded from the definition of *regulated mortgage contract* if, at the time it is entered into, it meets the following conditions:

 - (1) it meets the conditions in **■ PERG 4.4.1G (1)** to **■ (3)**; and
 - (2) the lender provides the borrower with credit exceeding £25,000; and
 - (3) the mortgage ranks in priority behind one or more other mortgages affecting the land in question; and
 - (4) the agreement is entered into by the borrower wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by the borrower.
- 4.4.22** **G** The *Regulated Activities Order* refers to this as a “second charge business loan”.
- 4.4.23** **G** (1) There is no exclusion from the £25,000 floor in **■ PERG 4.4.21G (2)** for an item entering into the *total charge for credit*.

(2) Giving time for payment of interest if the borrower gets into difficulty, does not affect the calculation of the sum as the definition relates to the time at which the contract is entered into.

(3) However, for example, if the credit includes a broker fee, that fee may be excluded in the calculation of the floor.

Exclusion for lending by credit unions

- 4.4.24 **G** A contract is excluded from the definition of *regulated mortgage contract* if, at the time it is entered into, it meets the following conditions:
- (1) it meets the conditions in ■ PERG 4.4.1G (1) to ■ (3); and
 - (2) the lender is a *credit union*; and
 - (3) it is a *borrower-lender agreement*; and
 - (4) the mortgage ranks in priority behind one or more other mortgages affecting the land in question; and
 - (5) the rate of the *total charge for credit* does not exceed 42.6 per cent.

4.4.25 **G** The *Regulated Activities Order* refers to this as a “limited interest second charge credit union loan”.

- 4.4.26 **G** The exclusion in ■ PERG 4.4.24 G only applies if the loan meets the following conditions:
- (1) the borrower receives timely information on the main features, risks and costs of the contract at the pre-contractual stage; and
 - (2) any advertising of the contract is fair, clear and not misleading.

Exclusion for second charge bridging loans

- 4.4.27 **G** A contract is excluded from the definition of *regulated mortgage contract* if, at the time it is entered into, it meets the following conditions:
- (1) it meets the conditions in ■ PERG 4.4.1G (1) to ■ (3); and
 - (2) it is a *borrower-lender-supplier agreement* financing the purchase of land; and
 - (3) it is used by the borrower as a temporary financing solution while changing to another financial arrangement for the land secured by the mortgage; and
 - (4) the mortgage ranks in priority behind one or more other mortgages affecting the land in question; and
 - (5) the number of payments to be made by the borrower under the contract is not more than four.

4.4.28 **G** The *Regulated Activities Order* refers to this as a “limited payment second charge bridging loan”.

Exclusion for equitable mortgage bridging loans

- 4.4.28A **G** A contract is excluded from the definition of *regulated mortgage contract* if, at the time is entered into, it meets the following conditions:

- (1) it is a *bridging loan* described in ■ PERG 4.13.6G;
- (2) it is secured by an equitable mortgage on *land*; and
- (3) it is an exempt agreement within the meaning of article 60B(3) (*regulated credit agreements*) of the *Regulated Activities Order* by virtue of article 60E(2): in summary, the *lender* is a *local authority*, or the agreement is specified in ■ CONC App 1.3 and the *lender* is a person or within class of persons specified in ■ CONC App 1.3 (see ■ PERG 2.7.19FG(1) and (2)).

4.4.28B G The *Regulated Activities Order* refers to such a contract as an 'exempt equitable mortgage bridging loan'.

Exclusion for housing association and other housing authority loans

4.4.28C G A contract is excluded from the definition of *regulated mortgage contract* if, at the time it is entered into, it meets the following conditions:

- (1) it provides for credit to be granted by a 'housing authority' within the meaning of article 60E of the *Regulated Activities Order*. The definition in article 60E includes housing associations registered under the relevant housing legislation (see ■ PERG 2.7.19FAG);
- (2) if entered into on or after 21 March 2016:
 - (a) it is an agreement of a kind to which the *MCD* does not apply by virtue of article 3(2) of the *MCD* (in other words, it is an agreement listed in ■ PERG 4.10A.5G(1) to (6)); or it is a *credit agreement* which relates to the deferred payment, free of charge, of an existing debt and is not secured by a *legal or equitable mortgage*; or
 - (b) it is a *bridging loan* described in ■ PERG 4.13.6G; or
 - (c) it is a restricted public loan described in ■ PERG 4.13.7G.

4.4.28D G The *Regulated Activities Order* refers to such a contract as an 'exempt housing authority loan'.

Certificate that borrower is not a consumer

4.4.29 G The two exclusions for loans to commercial borrowers (■ PERG 4.4.17 G and ■ PERG 4.4.21 G) depend on the borrower not being a consumer. For these purposes, if an agreement includes a declaration which:

- (1) is made by the borrower; and
- (2) includes:
 - (a) a statement that the agreement is entered into by the borrower wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by the borrower;
 - (b) a statement that the borrower understands that the borrower will not have the benefit of the protection and remedies that

would be available to the borrower under the *Act* if the agreement were a *regulated mortgage contract* under the *Act*; and

- (c) a statement that the borrower is aware that if the borrower is in any doubts as to the consequences of the agreement not being regulated by the *Act*, then the borrower should seek independent legal advice;

the agreement is to be presumed to have been entered into by the borrower wholly or predominantly for the purposes specified in (2)(a).

4.4.30 G However, the presumption in ■ PERG 4.4.29 G does not apply if, when the agreement is entered into:

- (1) the lender (or, if there is more than one lender, any of the lenders); or
- (2) any *person* who has acted on behalf of the lender (or, if there is more than one lender, any of the lenders) in connection with the entering into of the agreement;

knows, or has reasonable cause to suspect, that the agreement is not entered into by the borrower wholly or predominantly for the purposes of a business carried on, or intended to be carried on, by the borrower.

Exclusion for certain consumer buy-to-let mortgage contracts

4.4.31 G There is an exclusion for what the *RAO* refers to as an “exempt consumer buy-to-let mortgage contract”. This is explained in ■ PERG 4.10B (Regulation of buy-to-let lending).

4.4.32 G For a *buy-to-let credit agreement* (described in ■ PERG 4.10B.5G), article 61A(5) of the *Regulated Activities Order* says that a borrower is to be regarded as entering into an agreement, or intending to enter into an agreement, for the purposes of a business if (1) or (2) are met:

- (1) (a) the borrower previously purchased, or is entering into the contract in order to finance the purchase by the borrower of, the land secured by the mortgage;
- (b) at the time of the purchase the borrower intended that the land would be occupied as a dwelling on the basis of a rental agreement and would not at any time be occupied as a dwelling by the borrower or by a *related person* (see ■ PERG 4.4.19G), or where the borrower has not yet purchased the land the borrower has such an intention at the time of entering into the contract; and
- (c) where the borrower has purchased the land, since the time of the purchase the land has not at any time been occupied as a dwelling by the borrower or by a *related person* (see ■ PERG 4.4.19G);
- (2) the borrower is the owner of land, other than the land secured by the mortgage, which is

- (a) occupied as a dwelling on the basis of a rental agreement and is not occupied as a dwelling by the borrower or by a *related person* (see ■ PERG 4.4.19G); or
- (b) secured by a mortgage under a *buy-to-let credit agreement*.